

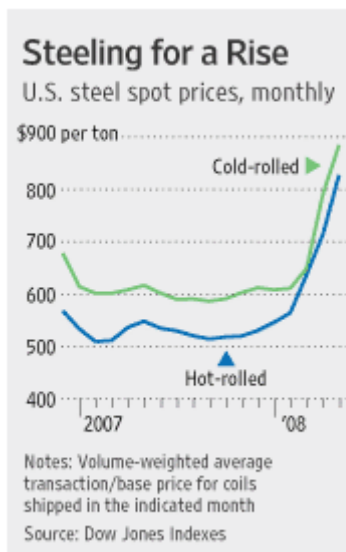
Rio Tinto and BHP Push the Cost of Iron Ore Higher

Steel Prices Fuel Inflation Worries; Taking a Hard Line

by ROBERT GUY MATTHEWS, THE WALL STREET JOURNAL

June 24, 2008 – Page B1

After months of negotiating with China's top steelmakers, mining giants Rio Tinto PLC and BHP Billiton Ltd. on Monday won an 85% increase in the benchmark price for iron ore, a key ingredient in steel production. The rise indicates that steel prices world-wide are likely to stay high, further fanning inflation concerns.



The increase -- which tops the amount that the companies' Brazilian rival Cia. [Vale do Rio Doce](#), known as Vale, negotiated for itself earlier in the year -- was settled between the mining companies and Baosteel Group Co., China's largest steelmaker, but will apply to all steelmakers that buy iron ore from the two, including U.S. and European customers. The BHP-Baosteel agreement hasn't been made public, but people familiar with the matter say BHP's iron-ore-price increase will be identical to Rio's publicly announced deal for an 85% rise.

The increase is retroactive to April 1. That means steelmakers that have purchased iron ore from BHP and Rio since then will have to write checks for the difference, which is likely to total hundreds of millions of dollars. Contract prices for iron ore, with this new increase, would be in the range of about \$140 a metric ton, up from about \$85 a ton.

With Monday's accord, Rio Tinto and BHP broke with the tradition of allowing one miner and one steelmaker to negotiate an agreed-upon price that would apply to all. Instead of accepting terms Vale negotiated earlier this year with Baosteel, BHP and Rio decided to work toward a deal of their own.

For Rio, taking a hard line in negotiations was important not only to boost profits, but also to help either fend off a bid from BHP or force BHP to boost its offer beyond 3.4 shares of BHP stock for one share of Rio Tinto. BHP first bid for Rio in November; in February, Rio rejected a sweetened offer on the grounds that it undervalued the company. The offer is now valued at \$171.51 billion, making it the world's largest pending takeover.

"We are much larger than BHP in terms of iron ore," said Sam Walsh, chief executive of Rio Tinto's iron-ore division, adding that the price rise "will provide a sizable uplift in our earnings." Iron-ore operations produce nearly 30% of Rio's earnings, compared with only about 15% of BHP's.

BHP Chief Executive Marius Kloppers said the negotiations' outcome validates arguments about the value of Australian iron ore, but he declined to discuss further implications. "I wouldn't care to speculate on the knock-on effects," he said.

For steelmakers, the news isn't good, though it wasn't entirely unexpected. There are just three major mining companies. The dozens of steelmakers face more competition and thus have little leverage on prices.

Baosteel said its prices will rise as a result of the iron-ore price increase, but it gave no estimates. Including the latest increase, Baosteel said iron ore will account for 65% of its raw-material costs. The price increase affects all iron-ore buyers, though U.S. steelmakers are less affected, as they can import ore more cheaply from Brazil.

At least one steelmaker is happy with the outcome. ArcelorMittal, the world's largest steelmaker by revenue and output, settled earlier this year with Vale on long-term contracts at a 65%-to-71% price increase.

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